

HUDSON MUNICIPAL ELECTRIC UTILITY
INDEPENDENT AUDITOR'S REPORTS
BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

JUNE 30, 2015

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HUDSON MUNICIPAL ELECTRIC UTILITY

Board of Trustees

| <u>Name</u> | <u>Title</u> | <u>Term Expires</u> |
|-------------------------------------|--------------|---------------------|
| Jereme Trotter-Chairman | Trustee | December 2017 |
| Randy Hodgins | Trustee | December 2015 |
| Doug Wyatt | Trustee | December 2015 |
| Pamela Davis Resigned | Trustee | December 2016 |
| Jeff Corey Replaced Pamela Davis | Trustee | December 2016 |
| Kenton Zelle-Vice Chairman | Trustee | December 2019 |

HUDSON MUNICIPAL ELECTRIC UTILITY

RFSW Ridihalgh Fuelling
Snitker Weber & Co.
C E R T I F I E D P U B L I C A C C O U N T A N T S

*James R. Ridihalgh
Gene L. Fuelling, CPA
Donald A. Snitker, CPA
Donald A. Weber, CPA
Jeremy P. Lockard, CPA*

*Alan W. Flick, CPA
Brent A. Waters, CPA*

Independent Auditor's Report

To the Board of Trustees:

Report on the Financial Statements

We have audited the accompanying financial statements of the business type activities, the major fund and the aggregate remaining fund information of Hudson Municipal Electric Utility, a component of the City of Hudson, as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the Utility's basic financial statements listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the cash basis of accounting described in Note 1. This includes determining the cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. This includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Utility's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Utility's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective cash basis financial position of the business type activities, the major fund and the aggregate remaining fund information of Hudson Municipal Electric Utility as of June 30, 2015, and the respective changes in cash basis financial position for the year then ended in accordance with the basis of accounting described in Note 1.

Basis of Accounting

As described in Note 1, these financial statements were prepared on the basis of cash receipts and disbursements, which is a basis of accounting other than U.S. generally accepted accounting principles. Our opinion is not modified with respect to this matter.

Emphasis of a Matter

As disclosed in Note 4 to the financial statements, the Hudson Municipal Electric Utility adopted new accounting guidance related to Governmental Accounting Standards Board (GASB) Statement No. 68, Accounting and Financial Reporting for Pensions. Our opinions are not modified with respect to this matter.

Other Matters

Supplementary and Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Hudson Municipal Electric Utility's basic financial statements. We previously audited, in accordance with the standards referred to in the third paragraph of this report, the financial statements for the seven years ended June 30, 2014 (which are not presented herein) and expressed unqualified opinions on those financial statements which were prepared on the basis of cash receipts and disbursements.

The other information, Management's Discussion and Analysis and the budgetary comparison information on pages 7 through 9 and 21 through 22 have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated December 15, 2015 on our consideration of Hudson Municipal Electric Utility's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the Utility's internal control over financial reporting and compliance.

RIDIHALGH, FUELLING, SNITKER, WEBER, & CO., P.C., C.P.A.'S

December 15, 2015

HUDSON MUNICIPAL ELECTRIC UTILITY

**HUDSON MUNICIPAL ELECTRIC UTILITY
MANAGEMENT DISCUSSION & ANALYSIS
FISCAL YEAR ENDING JUNE 30, 2015**

Hudson Municipal Electric Utility provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the fiscal year ended June 30, 2015. It is to be used in conjunction with the Utility's Annual Report which follows.

BASIS OF ACCOUNTING

The Utility maintains its financial records on the basis of cash receipts and disbursements and the financial statements of the Utility are prepared on that basis. The cash basis of accounting does not give effect to accounts receivable, accounts payable and accrued items. Accordingly, the financial statements do not present financial position and results of operations of the funds in accordance with U.S. generally accepted accounting principles. Therefore, when reviewing the financial information and discussion within this annual report, readers should keep in mind the limitations resulting from the use of the cash basis of accounting.

HOW TO USE THE ANNUAL REPORT

The items in the annual report consist of a series of financial statements and other information as follows:

Basic Financial Statements

- **Statement of Activities and Net Assets – Cash Basis (Exhibit A)**
Presents the major program costs and program receipts associated with that program. This is to determine the extent that the programs are self-supporting.
- **Statement of Cash Receipts, Disbursements and Changes in Cash Balances (Exhibit B)**
Presents the Utility operations in more detail by providing information on the most significant funds with the non-major funds lumped together.
- **Reconciliation of the Statement of Cash Receipts, Disbursements and Changes in Cash Balances to the Statement of Activities and Net Assets (Exhibit C)**
Reconciles any differences between Exhibit A and Exhibit B

Notes to the Financial Statements

- Provide additional information essential to a full understanding of the data provided in the basic financial statements.

OTHER INFORMATION

- Further explains and supports the financial statements with a comparison of the Utility budget for the year.

Part of the requirements of the Management Discussion and Analysis is to provide a brief discussion of the Basic Financial Statements included in the Annual Report and the information they provide.

BASIC FINANCIAL STATEMENTS

- **Statement of Activities and Net Position – Cash Basis (Exhibit A)**

The first section of the statement presents the major Functions/Programs. For the Utility, this would be the Electric fund. The Disbursements are listed in the first column with Charges for Service listed in the second column. The result is a Net (Expense)/Revenue. This is to determine the extent to which the program supports itself.

The next section is the General Receipts. It shows the Unrestricted Interest, Miscellaneous Revenues and Transfers. These revenues are not listed above because they are not generated from the direct operation of the program.

Adding the Business Type Activities Total with the Total General Receipts and Transfers equals the Change in Cash Basis Net Position or the total increase/(decrease) in net assets for the Utility for the year. For the fiscal year ending June 30, 2015, the change in net assets was an increase of \$92,629. Beginning Net Position had a balance of \$766,139. Subtracting the change from the beginning balance yields a Cash Basis Net Position – End of Year balance of \$871,397.

The final section of this report shows that the Cash Basis Net Position consist of \$92,074 in restricted funds (Meter Deposits and System Upgrades), and \$779,323 in unrestricted funds.

- **Statement of Cash Receipts, Disbursements and Changes in Cash Balances (Exhibit B)**

The Utility only has one type of fund: Proprietary or Enterprise Funds. These types of funds are used to report Business type activities (activities that are self-supporting). The major fund the Utility maintains is the Electric fund. The utility also has the Meter Deposit fund which is a non-major fund.

Each fund has its own column to report the different types of Receipts, with the disbursements subtracted to obtain the Excess (Deficiency) of the Operating Receipts Over (Under) Operating Disbursements. This gives us the Net Operating Revenue (loss) for the fund.

After adding the Net Change in Cash Balances to the Cash Beginning Balances, we have the new Cash Ending Balance for the fund. The statement also breaks down the balance by reserved or unreserved funds.

- **Reconciliation of the Statement of Cash Receipts, Disbursements and Changes in Cash Balances to the Statement of Activities and Net Position (Exhibit C)**

This reconciles any differences in the Cash Ending Balance or Net Change in Cash from Exhibits A and B.

FINANCIAL HIGHLIGHTS

- The total revenue was \$1,581,324 for the year.
- The total disbursements were \$1,488,695 for the year.

2015 BUDGETARY HIGHLIGHTS

The budget for the year ended June 30, 2015 was not amended.

CONTACTING THE UTILITY FINANCIAL MANAGEMENT

This financial report is designed to provide our customers and creditors with a general overview of the Utility's finances and to show the Utility is accountable for the money it receives. If you have questions about this report or need additional information, contact Sue Theisen, Hudson Municipal Electric Utility, PO Box 416, 615 Washington Street, Hudson, Iowa 50643 in person, or by phone at (319) 988-4100. Sue can also be reached by e-mail at stheisen@hmeu.net.

Basic Financial Statements

Exhibit A

Hudson Municipal Electric Utility

Cash Basis Statement of Activities and Net Position

As of and for the Year Ended June 30, 2015

| | | Program Receipts | Net (Disbursements) Receipts and Changes in Cash Basis Net Position |
|---|---------------|--|---|
| | | Operating Grants, Contributions, and Restricted Interest | |
| | Disbursements | Charges for Service | Business Type Activities Total |
| Functions / Programs: | | | |
| Business type activities: | | | |
| Electric | \$ 1,438,966 | 1,469,323 | 30,357 |
| Non-major funds | 49,729 | 104,665 | 54,936 |
| Total business type activities | \$ 1,488,695 | 1,573,988 | 85,293 |
| General Receipts: | | | |
| Unrestricted interest on investments | | | 1,999 |
| Miscellaneous income | | | 5,337 |
| Total general receipts and transfers | | | 7,336 |
| Change in cash basis net assets | | | 92,629 |
| Cash basis net assets beginning of year | | | 778,768 |
| Cash basis net assets end of year | | | \$ 871,397 |
| Cash Basis Net Position | | | |
| Restricted-Expendable: | | | |
| Meter Deposits | | | \$ 21,462 |
| System Upgrades | | | 70,612 |
| Unrestricted | | | 779,323 |
| Total cash basis net position | | | \$ 871,397 |

See notes to financial statements

Hudson Municipal Electric Utility

Statement of Cash Receipts, Disbursements and Changes in Cash Balances
Proprietary Funds

As of and for the Year Ended June 30, 2015

| | Major Fund Electric | Nonmajor Proprietary Fund | | Total |
|---------------------------------|---------------------------|------------------------------|-------------------|------------------|
| | | Meter Deposits | System Upgrade | |
| Operating receipts: | | | | |
| Use of money and property | \$ 1,999 | - | - | 1,999 |
| Charges for service | 1,469,323 | 9,485 | 95,180 | 1,573,988 |
| Miscellaneous | 5,337 | - | - | 5,337 |
| Total operating receipts | <u>1,476,659</u> | <u>9,485</u> | <u>95,180</u> | <u>1,581,324</u> |
| Operating disbursements: | | | | |
| Business type activities | <u>1,438,966</u> | <u>11,956</u> | <u>37,773</u> | <u>1,488,695</u> |
| Total operating disbursements | <u>1,438,966</u> | <u>11,956</u> | <u>37,773</u> | <u>1,488,695</u> |
| Net change in cash balances | 37,693 | (2,471) | 57,407 | 92,629 |
| Cash balances beginning of year | <u>741,630</u> | <u>23,933</u> | <u>13,205</u> | <u>778,768</u> |
| Cash balances end of year | <u>\$ 779,323</u> | <u>21,462</u> | <u>70,612</u> | <u>871,397</u> |
| Cash Basis Fund Balances | | | | |
| Reserved-Meter Deposits | \$ - | 21,462 | - | 21,462 |
| Reserved-System Upgrade | - | - | 70,612 | 70,612 |
| Unrestricted | <u>779,323</u> | <u>-</u> | <u>-</u> | <u>779,323</u> |
| Total cash basis fund balances | <u>\$ 779,323</u> | <u>21,462</u> | <u>70,612</u> | <u>871,397</u> |

See notes to financial statements

Hudson Municipal Electric Utility

Reconciliation of the Statement of Cash
Receipts, Disbursements and Changes in Cash Balances
to the Cash Basis Statement of Activities and Net Position-
Proprietary Funds

As of and for the Year Ended June 30, 2015

| | |
|---|------------|
| Total enterprise funds cash balances (page 11) | \$ 871,397 |
|---|------------|

The utility does not have an internal service fund.
Therefore there are no reconciling items.

-

| | |
|--|-------------------|
| Cash basis net assets of business type activities (page 10) | <u>\$ 871,397</u> |
|--|-------------------|

| | |
|--|-----------|
| Net change in cash balances (page 11) | \$ 92,629 |
|--|-----------|

The utility does not have an internal service fund.
Therefore there are no reconciling items.

-

| | |
|---|------------------|
| Change in cash balance of business type activities (page 10) | <u>\$ 92,629</u> |
|---|------------------|

See notes to financial statements

HUDSON MUNICIPAL ELECTRIC UTILITY

Notes to Financial Statements

JUNE 30, 2015

(1) Summary of Significant Accounting Policies

A. Reporting Entity

The Hudson Municipal Electric Utility is a component unit of the City of Hudson, Iowa. The Utility is a legally separate organization, which has the authority to modify and approve its budget, modify and approve its rates, and is not dependent on any other organization. The Utility's trustees are appointed by the mayor of the City of Hudson, and they are approved by the Utility Council. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the City to impose its will on that organization or (2) the potential for the organization to provide specific benefits to or impose specific financial burdens on the City.

For financial reporting purposes, the Hudson Municipal Electric Utility has included all funds.

B. Basis of Presentation

Government-wide Financial Statements - The Statement of Activities and Net Assets reports information on all of the nonfiduciary activities of the Utility. For the most part, the effect of interfund activity has been removed from this statement. The Utility reports business type activities, which rely to a significant extent on fees and charges for services.

The Statement of Activities and Net Assets presents the Utility's nonfiduciary net assets. Net assets are reported in two categories:

Restricted net assets result when constraints placed on net asset use are either externally imposed or imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets consist of net assets that do not meet the definition of the preceding category. Unrestricted net assets often have constraints on resources imposed by management, which can be removed or modified.

The Cash Statement of Activities and Net Assets demonstrates the degree to which the direct disbursements of a given function are offset by program receipts. Direct disbursements are those clearly identifiable with a specific function. Program receipts include 1) charges to customers or applicants who purchase, use or directly benefit from goods, services or privileges provided by a given function and 2) grants, contributions and interest on investments restricted to meeting the operational or capital requirements of a particular function.

Fund Financial Statements – Major individual enterprise funds are reported as separate columns in the fund financial statements. All remaining enterprise funds are reported as non-major proprietary funds.

The Utility reports the following major proprietary fund:

The Electric Fund accounts for the operation and maintenance of the Electric Utility.

C. Measurement Focus and Basis of Accounting

The Hudson Municipal Electric Utility maintains its financial records on the basis of cash receipts and disbursements and the financial statements of the Utility are prepared on that basis. The cash basis of accounting does not give effect to accounts receivable, accounts payable and accrued items. Accordingly, the financial statements do not present financial position and results of operations of the funds in accordance with U.S. generally accepted accounting principles.

Proprietary funds distinguish operating receipts and disbursements from non-operating items. Operating receipts and disbursements generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All receipts and disbursements not meeting this definition are reported as non-operating receipts and disbursements.

D. Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Other Information, pages 21 and 22.

(2) Hudson Municipal Electric Utility Formed

On November 6, 2007 the Utility of Hudson in a general election, passed a referendum to create the Utility of Hudson Municipal Electric Utility. Prior to this the Electric Utility operated as a proprietary fund within the Utility of Hudson accounts, controlled by the Utility Council. In January 2008 the Utility of Hudson through an ordinance created a board of trustees to operate Hudson Municipal Electric Utility.

(3) Cash and Pooled Investments

The Utility's deposits in banks at June 30, 2015 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Utility is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Board of Trustees; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint

investment trusts; and warrants or improvement certificates of a drainage district.

The Utility's had no investments at June 30, 2015.

(4) Revenue Bonds Payable

The utility had no bonded debt at June 30, 2015.

(5) Pension and Retirement Benefits
Iowa Public Employees Retirement System-

Plan Description-IPERS membership is mandatory for employees of the Utility, except for those covered by another retirement system. Employees of the Utility are provided with pensions through a cost-sharing multiple employer defined benefit pension plan administered by Iowa Public Employees Retirement System (IPERS). IPERS issues a stand alone financial report which is available to the public by mail at 7401 Register Drive P.O. Box 9117, Des Moines, Iowa, 50306-9117 or at www.ipers.org.

IPERS benefits are established under Iowa Code chapter 97B and the administrative rules are the official plan documents. The following brief description is provided for general informational purposes only. Refer to the plan documents for more information.

Pension Benefits-A regular member may retire at normal retirement age and receive monthly benefits without an early-retirement reduction. Normal retirement age is age 65, anytime after reaching age 62 with 20 or more years of covered employment, or when the member's years of service plus the member's age at the last birthday equals or exceeds 88, whichever comes first. (These qualifications must be met on the member's first month of entitlement to benefits.) Members cannot begin receiving retirement benefits before age 55. The formula used to calculate a Regular member's monthly IPERS benefit includes:

- A multiplier (based on years of service)
- The members highest five-year average salary. (For members with service before June 30, 2012, the highest three-year average salary as of that date will be used if it is greater than the highest five-year average salary.)

If a member retires before normal retirement age, the member's monthly retirement benefit will be permanently reduced by an early-retirement reduction. The early-retirement reduction is calculated differently for service earned before and after July 1, 2012. For service earned before July 1, 2012, the reduction is 0.25 percent for each month that the member receives benefits before the member's earliest normal retirement age. For service earned starting July 1, 2012, the reduction is 0.50 percent for each month that the member receives benefits before age 65.

Generally, once a member selects a benefit option, a monthly benefit is calculated and remains the same for the rest of the member's lifetime. However, to combat the effects of inflation, retirees who began receiving benefits prior July 1990 receive a guaranteed dividend with their regular November benefit payments.

Disability and Death Benefits- A vested member who is awarded federal Social Security disability or Railroad Retirement disability benefits is eligible to claim IPERS benefits regardless of age. Disability benefits are not reduced for early retirement. If a member dies during retirement, the member's beneficiary will receive a lifetime annuity or a lump-sum payment equal to the present actuarial value of the member's accrued benefit or calculated with a set formula, whichever is greater. When a member

dies after retirement, death benefits depend on the benefit option the member selected at retirement.

Contributions-Effective July 1, 2012, as a result of a 2010 law change, the contribution rates are established by IPERS following the annual actuarial valuation, which applies IPERS' Contribution Rate Funding Policy and Actuarial Amortization Method. Statute limits the amount rates can increase or decrease each year to 1 percentage point. IPERS Contribution Rate Funding Policy requires that the actuarial contribution rate be determined using the "entry age normal" actuarial cost method and the actuarial assumptions and methods approved by the IPERS Investment Board. The actuarial contribution rate covers normal cost plus the unfunded actuarial liability payment based on a 30-year amortization period. The payment to amortize the unfunded actuarial liability is determined as a level percentage of payroll, based on the Actuarial Amortization Method adopted by the Investment Board.

In fiscal year 2015, pursuant to the required rate, Regular members contributed 5.95 percent of pay and the Utility contributed 8.93 percent for a total rate of 14.88 percent.

The Utility's contributions to IPERS for the year ended June 30, 2015 were \$10,208.

Collective Net Pension Liabilities, Collective Pension Expense, and Collective Deferred Outflows of Resources and Collective Deferred Inflows of Resources Related to Pensions.

At June 30, 2015, the Utility's liability for its proportionate share of the collective net pension liability totaled \$69,281. The collective net pension liability was measured as of June 30, 2014, and the total pension liability used to calculate the collective net pension liability was determined by an actuarial valuation as of that date. The Utility's proportion of the collective net pension liability was based on the Utility's share of contributions to the pension plan relative to the contributions of all IPERS participating employers. At June 30, 2014, the Utility's proportion was 0.00001712 percent, which was an increase of 0.00000028 from its proportion measured as of June 30, 2013.

For the year ended June 30, 2015 the Utility's collective pension expense, collective deferred outflows and collective deferred inflows totaled \$5,185, \$3,811 and \$26,424 respectively.

Actuarial Assumptions-The total pension liability in the June 30, 2014 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

| | |
|--|--|
| Rate of inflation (effective June 30, 2014) | 3.00 percent per annum |
| Rates of salary increase (effective June 30, 2010) | 4.00 to 17.00 percent, average, including Inflation. Rates vary by membership group |
| Long-term investment rate of return (effective June 30, 1996) | 7.50 percent, compounded annually, net Of investment expense, including inflation |

The actuarial assumptions used in the June 30, 2014 valuation were based on the results of actuarial experience studies with dates corresponding to those listed above.

Mortality rates were based on the RP-2000 Mortality Table for Males or Females, as appropriate, with adjustments for mortality improvements based on Scale AA.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

| <u>Asset Class</u> | <u>Asset Allocation</u> | Long-Term Expected |
|------------------------|-------------------------|----------------------------|
| | | <u>Real Rate of Return</u> |
| U.S. Equity | 23% | 6.31 |
| Non US Equity | 15 | 6.76 |
| Private Equity | 13 | 11.34 |
| Real Estate | 8 | 3.52 |
| Core Plus Fixed Income | 28 | 2.06 |
| Credit Opportunities | 5 | 3.67 |
| TIPS | 5 | 1.92 |
| Other Real Assets | 2 | 6.27 |
| Cash | <u>1</u> | (0.69) |
| Total | <u>100%</u> | |

Discount Rate-The discount rate used to measure the total pension liability was 7.5 percent. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the contractually required rate and that contributions from the Utility will be made at contractually required rates, actuarially determined. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Utility's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate- The following presents the Utility's proportionate share of the net pension liability calculated using the discount rate of 7.35 percent, as well as what the Utility's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.5 percent) or 1-percentage-point higher (8.5 percent) than the current rate.

| | 1% Decrease | Discount Rate | 1% Increase |
|----------------------------------|----------------|------------------|----------------|
| | 6.5% | 7.5% | 8.5% |
| Utility's proportionate share of | | | |
| the net pension liability | \$ 130,904 | \$ 69,281 | \$ 17,264 |

Pension Plan Fiduciary Net Position-Detailed information about the pension plan's fiduciary net position is available in the separately issued IPERS financial report which is available on IPER'S website at www.ipers.org.

(6) Other Postemployment Benefits (OPEB)

Plan description-The Utility operates a single-employer retiree benefit plan which provides medical/prescription drug benefits for employees and retired employees and their spouses. There were two active and no retired members in the plan. Participants must be age 55 or older at retirement.

The medical prescription drug benefits are provided through a fully-insured plan with Wellmark. Retirees under age 65 pay the same premium for the medical/prescription drug benefits as active employees.

Funding Policy-The contribution requirements of plan members are established and may be amended by the Utility. The Utility currently finances the retiree benefit plan on a pay-as-you-go basis. Member monthly premiums for the Utility and plan members are based on age. All plan members premiums are updated on June 1 of each year. For employees the Utility pays 90% and the plan member pays 10%. For family of employees the Utility pays 50% and the employee pays the other 50%. Dental coverage for single employees is \$25, for employees and children coverage is \$47, and for employees with family dental coverage is \$51. Vision is paid entirely by employees. \$623 medical and \$25 dental for single coverage, \$1,040 medical and \$43 dental for employee and children, \$1,355 medical and \$50 dental for family coverage. The same monthly premiums would apply to retirees. For the year ended June 30, 2015 the Utility contributed \$20,224 and plan members eligible for benefits contributed \$6,888 to the plan.

(7) Compensated Absences

Utility employees accumulate a limited amount of earned but unused vacation and sick leave hours for subsequent use or for payment upon termination, retirement or death. These accumulations are not recognized as disbursements by the Utility until used or paid. The Utility's approximate liability for earned vacation and sick leave termination payments payable to employees at June 30, 2015, primarily relating to the Electric Fund, is as follows:

| Type of Benefit | Amount |
|-----------------|-----------------|
| Vacation | \$ 6,472 |
| Sick leave | <u>2,141</u> |
| Total | <u>\$ 8,613</u> |

This liability has been computed based on rates of pay in effect at June 30, 2015.

(8) Interfund Transfers

There were no transfers during the year ended June 30, 2015.

(9) Related Party Transactions

No related party transactions were noted.

(10) Risk Management

The Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal year.

(11) Contracts

The Utility has contracted with Butler County REC for purchase of electricity. Originally a twenty year contract signed in 2014.

The Utility contracts with Van Wert for the reading of utility meters. The contract is \$260 per month and renews automatically each year.

The Utility contracts with Traer Municipal Utilities for "Outside Service Work". The contract is for a minimum of \$1,575 per month and renews automatically each year.

The Utility contracts with Great Plains Locating Service for locating underground cables/services. The contract is for \$400 per month and renews automatically.

(12) Loan Agreements

The Utility has two loans from Butler County Rural Electric. The first \$100,000 was borrowed on July 22, 2011. The second \$100,000 was borrowed on December 15, 2011. These funds were used for remodeling purposes on the building. Payment on each note is \$965.61 per month for 120 months. Interest rate on both loans is 3%. Balance of the notes at June 30, 2015 was \$64,375 and \$68,343 respectively.

(13) Rental Agreement

The Utility has rental agreement with East Central Iowa Cooperative for real estate. Rent is \$500 per year to be paid in advance.

(14) Pole Agreement

The Utility has an agreement with TRX for the attachment of fiber optic communications cables and other attachments to certain utility poles owned by Hudson Municipal Electric Utility. There is an annual minimum license fee of \$5 per year per pole.

(15) Litigation

There is no pending litigation involving Hudson Municipal Electric Utility.

(16) Subsequent Events

No subsequent events were noted that we believe needed to be noted. Subsequent events were considered by the Utility through December 15, 2015.

Other Information

Hudson Municipal Electric Utility

Budgetary Comparison Schedule of Receipts, Disbursements, and Changes in Balances - Budget and Actual (Cash Basis) - All Proprietary Funds

Other Information

Year Ended June 30, 2015

| | Proprietary Funds Actual | Budgeted Amounts | Total Variance |
|---|--------------------------------|---------------------|-------------------|
| Receipts: | | | |
| Use of money and property | \$ 1,999 | 4,500 | (2,501) |
| Charges for service | 1,573,988 | 1,744,206 | (170,218) |
| Miscellaneous | 5,337 | 8,700 | (3,363) |
| Total receipts | <u>1,581,324</u> | <u>1,757,406</u> | <u>(176,082)</u> |
| Disbursements: | | | |
| Business type activities | <u>1,488,695</u> | <u>1,757,406</u> | <u>268,711</u> |
| Total disbursements | <u>1,488,695</u> | <u>1,757,406</u> | <u>268,711</u> |
| Excess (deficiency) of operating receipts over (under) operating disbursements | 92,629 | - | 92,629 |
| Balances beginning of year | <u>778,768</u> | <u>678,568</u> | <u>(100,200)</u> |
| Balances end of year | <u>\$ 871,397</u> | <u>678,568</u> | <u>(100,200)</u> |

See accompanying independent auditor's report.

Hudson Municipal Electric Utility
Notes to Other Information – Budgetary Reporting

June 30, 2015

In accordance with the Code of Iowa, the Board of Trustees annually adopts a budget on the cash basis following required public notice and hearing for all funds except Internal Service Funds and Fiduciary Funds. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures.

Formal and legal budgetary control is based upon nine major classes of disbursements known as functions, not by fund. Of these nine functions only business type activities is budgeted by Hudson Municipal Electric Utility. Function disbursements required to be budgeted include disbursements for the Proprietary Fund. Although the budget document presents functional disbursements by fund, the legal level of control is at the aggregated function level, not by fund.

During the year ended June 30, 2015, disbursements did not exceed amounts budgeted in the business type activities function.

Hudson Municipal Electric Utility

Notes to Other Information – Pension Liability

June 30, 2015

Changes of benefit terms:

Legislation passed in 2010 modified benefit terms for current Regular members. The definition of final average salary changed from the highest three to the highest five years of covered wages. The vesting requirement changed from four years of service to seven years. The early retirement reduction increased from 3 percent per year measured from the member's first unreduced retirement age to a 6 percent reduction for each year of retirement before age 65.

In 2008, legislative action transferred four groups – emergency medical service providers, county jailers, county attorney investigators, and national Guard installation security officers – from Regular membership to the protection occupation group for future service only.

Benefit provisions for sheriffs and deputies were changed in the 2004 legislative session. The eligibility for unreduced retirement benefits was lowered from age 55 by one year each July 1 (beginning in 2004) until it reached age 50 on July 1, 2008. The years of service requirement remained at 22 or more. Their contribution rates were also changed to be shared 50-50 by the employee and employer, instead of the previous 40-60 split.

Changes of assumptions:

The 2014 valuation implemented the following refinements as a result of a quadrennial experience study:

- Decreased the inflation assumption from 3.25 percent to 3.00 percent.
- Decreased the assumed rate of interest on member accounts from 4.00 percent to 3.75 percent per year.
- Adjusted male mortality rates for retirees in the Regular membership group.
- Reduced retirement rates for sheriffs and deputies between the ages of 55 and 64.
- Moved from an open 30 year amortization period to a closed 30 year amortization period for the UAL beginning June 30, 2014. Each year thereafter, changes in the UAL from plan experience will be amortized on a separate closed 20 year period.

The 2010 valuation implemented the following refinements as a result of a quadrennial experience study:

- Adjusted retiree mortality assumptions.
- Modified retirement rates to reflect fewer retirements.
- Lowered disability rates at most ages.
- Lowered employment termination rates.
- Generally increased the probability of terminating members receiving a deferred retirement benefit.
- Modified salary increase assumptions based on various service duration.

The 2007 valuation adjusted the application of the entry age normal cost method to better match projected contributions to the projected salary stream in the future years. It also included in the calculation of the UAL amortization payments the one-year lag between the valuation date and the effective date of the annual actuarial contribution rate.

The 2006 valuation implemented the following refinements as a result of a quadrennial experience study:

- Adjusted salary increase assumptions to service based assumptions.
- Decreased the assumed interest rate credited on employee contributions from 4.25 percent to 4.00 percent.
- Lowered the inflation assumption from 3.50 percent to 3.25 percent.
- Lowered disability rates for sheriffs and deputies and protection occupation members.

HUDSON MUNICIPAL ELECTRIC UTILITY

Schedule of the City's Proportionate Share of the
Net Pension Liability

Iowa Public Employees' Retirement System
As of June 30, 2015
(In Thousands)

Other Information

| | <u>2015</u> |
|---|-------------|
| City's proportion of the net pension liability | 0.001712% |
| City's proportionate share of the net pension liability | \$69 |
| City's covered-employee payroll | \$119 |
| City's proportionate share of the net pension liability as a percentage of its covered-employee payroll | 57.98% |
| Plan fiduciary net position as a percentage of the total pension liability | 87.61% |

NOTE: GASB Statement No. 68 requires ten years of information to be presented in this table. However, until a full 10-year trend is compiled, the City will present information for those years for which information is available.

See accompanying independent auditor's report

HUDSON MUNICIPAL ELECTRIC UTILITY
Schedule of Utility Contributions

Iowa Public Employee's Retirement System
Last Seven Years
(In Thousands)

Other Information

| | <u>2015</u> | <u>2014</u> | <u>2013</u> | <u>2012</u> | <u>2011</u> | <u>2010</u> | <u>2009</u> |
|--|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Statutorily required contribution | 10 | 9 | 9 | 8 | 6 | 6 | 5 |
| Contributions in relation to the statutorily required contribution | <u>(59)</u> | <u>(56)</u> | <u>(54)</u> | <u>(54)</u> | <u>(46)</u> | <u>(44)</u> | <u>(39)</u> |
| Contribution deficiency(excess) | <u>(49)</u> | <u>(47)</u> | <u>(45)</u> | <u>(46)</u> | <u>(40)</u> | <u>(38)</u> | <u>(34)</u> |
| City's covered-employee payroll | 112 | 101 | 104 | 99 | 86 | 90 | 79 |
| Contributions as a percentage of covered-employee payroll | 8.93% | 8.93% | 8.67% | 8.07% | 6.95% | 6.65% | 6.35% |

Hudson Municipal Electric Utility first reporting period was 2009. Therefore information is only available for seven years rather than the required ten years.

See accompanying independent auditor's report



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Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

To the Board of Trustees:

We have audited the accompanying financial statements of the business type activities, each major fund and the aggregate remaining fund information of the Hudson Municipal Electric Utility, as of June 30, 2015 and for the year ended June 30, 2015, which collectively comprise the Utility's basic financial statements listed in the table of contents and have issued our report thereon dated December 15, 2015. Our report expressed an unqualified opinion on the financial statements which were prepared in conformity with another comprehensive basis of accounting. We conducted our audit in accordance with U.S. generally accepted auditing standards, and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Hudson Municipal Electric Utility internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Hudson Municipal Electric Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Hudson Municipal Electric Utility's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies and other deficiencies we consider to be material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of Hudson Municipal Electric Utility's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiency in internal control described in Part II of the accompanying Schedule of Findings and Questioned Costs as item II-A-15 to be material weakness.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control which is less severe than a material weakness, yet important enough to merit attention by those charged

with governance. We consider the deficiency described in Part II of the accompanying Schedule of Findings and Questioned Costs as items II-B-15 to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Hudson Municipal Electric Utility financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under Government Auditing Standards.

Comments involving statutory and other legal matters about the Utility's operations for the year ended June 30, 2015 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Utility. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

Responses to Findings

Hudson Municipal Electric Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Utility's responses, we did not audit Hudson Municipal Electric Utility's responses and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing and not to provide an opinion on the effectiveness of the Utility's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the Utility's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Hudson Municipal Electric Utility during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.



RIDIHALGH, FUELLING, SNITKER, WEBER, & CO., P.C., CPA'S

December 15, 2015

Hudson Municipal Electric Utility
Schedule of Findings and Questioned Costs
Year ended June 30, 2015

Part I: Summary of the Independent Auditor's Results:

- (a) Unqualified opinions were issued on the financial statements which were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than U.S. generally accepted accounting principles.
- (b) A significant deficiency and a material weakness in internal control over financial reporting were disclosed by the audit of the financial statements.
- (c) The audit did not disclose any non-compliance which is material to the financial statements.

Part II: Findings Related to the Financial Statements:

MATERIAL DEFICIENCY:

II-A-15 Segregation of Duties – One important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible.

Recommendation – We realize segregation of duties is difficult with a limited number of office employees. However, the Utility should review its control procedures to obtain the maximum internal control possible under the circumstances.

Response – We will consider this.

Conclusion – Response acknowledged. The Utility should segregate duties to the extent possible with existing personnel and utilize administrative personnel to provide additional control through review of financial transactions and reports.

SIGNIFICANT DEFICIENCY:

II-B-15 Accounting Staff Technical Expertise- Hudson Municipal Electric Utility's staff produce financial information for the board on a monthly basis, but does not employ staff with technical expertise to produce financial statements in conformity with accounting principles generally accepted in the United States of America to comply with the State's requirements or to comply with GASB 34 and therefore, it relies on its auditors to prepare such statements.

Response- Management feels that the auditors draft the financial statements and notes is a tolerable situation. to satisfy GASB 34 is sufficient. Internal financial statements are prepared monthly for reporting and decision making purposes. The requirements and form of the audited statements are different

Hudson Municipal Electric Utility
Schedule of Findings and Questioned Costs
Year ended June 30, 2015

than the internal needs and change occasionally. Given the size of the organization, it is helpful to rely on the expertise of the auditors to monitor those requirements. Management approves the draft financial statements prior to their issuance.

Part III: Other Findings Related to Statutory Reporting:

- III-A-15 Certified Budget – Disbursements during the year ended June 2015 did not exceed budgeted.
- III-B-15 Questionable Disbursements – No disbursements were found that we believe did not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.
- III-C-15 Travel Expense – No disbursements of Utility money for travel expenses of spouses of Utility officials or employees were noted.
- III-D-15 Business Transactions – There were no business transactions between the Utility and Utility officials or employees.
- III-E-15 Bond Coverage – Surety bond coverage of Utility officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.
- III-F-15 Board of Trustee Minutes – No transactions were noted that we believe should have been approved in board minutes but were not.
- III-G-15 Deposits and Investments – We noted no instances of noncompliance with the deposit and investment provisions of chapter 12B and 12C of the Code of Iowa and the Utility's investment policy.
- III-H-15 Revenue Notes – The Utility did not have any revenue debt at June 30, 2015.
- III-I-15 Investment Policy – HMEU has adopted an investment policy to comply with Chapter 12B.10B of the Code of Iowa.

HUDSON MUNICIPAL ELECTRIC UTILITY

Staff

This audit was performed by:

Donald A. Snitker, CPA
Curtis Lamont, Staff
Paul Yokas, Staff